

January 14, 2021

## Ajmer Vidyut Vitran Nigam Limited: Provisional [ICRA]BBB(CE)(Stable) rating assigned

### Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Proposed Bonds	500.00	Provisional [ICRA]BBB(CE)(Stable); Assigned
<b>Total</b>	<b>500.00</b>	

\* - Instrument details are provided in Annexure-1

<b>Rating Without Explicit Credit Enhancement</b>	<b>[ICRA]BB</b>
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Note: The (CE) suffix mentioned alongside the rating symbol indicates that the rated instrument/facility is backed by some form of explicit credit enhancement. This rating is specific to the rated instrument/facility, its terms and its structure and does not represent ICRA's opinion on the general credit quality of the entity concerned. The last row in the table above also captures ICRA's opinion on the rating without factoring in the explicit credit enhancement.

### Rationale

The provisional rating for the proposed bonds of Ajmer Vidyut Vitran Nigam Ltd (AVVNL) is based on the strength of the unconditional and irrevocable guarantee to be provided by the State Government of Rajasthan (GoR / Guarantor) as specified in the GoR order dated March 1, 2019 shared with ICRA. Since the guarantee document has not been shared with ICRA, the rating assigned is provisional as of now (as denoted by the prefix 'Provisional' before the rating symbol) and is subject to the fulfilment and review of all pending action/documentation pertaining to the instrument rated by ICRA. The final rating may differ from the provisional rating in case the completed action/documentation is not in line with ICRA's expectations.

The rating for AVVNL factors in the company's status as a wholly-owned power sector entity of the GoR and the support available from GoR in the form of equity, grant and guaranteed debt. The rating also takes into consideration the presence of the cost-plus tariff framework through the fuel surcharge mechanism which allows AVVNL to recover the uncontrollable cost variation on a quarterly basis. ICRA also notes the tariff hike approved by the Rajasthan Electricity Regulatory Commission (RERC) in February 2020 which is expected to result in an improvement in the cash flows of AVVNL and lower the revenue gap.

The rating is, however, constrained by the moderately high distribution loss level of AVVNL, although the same has improved gradually over the past few years post implementation of Ujjwal Discom Assurance Yojana (UDAY). The rating also takes into consideration the high absolute subsidy dependence for AVVNL on GoR (forms 20-23% of the revenue), implying that timely receipt of subsidy from the GoR remains critical. ICRA notes that while the subsidy receipts have been timely, the actual release of subsidy has remained lower than the actual claims over the years, leading to a build-up of pending subsidy dues to Rs. 2,738 crore till March 31, 2020. The rating is further constrained by the weak cost coverage ratio, high debt levels, negative networth due to large losses booked and weak debt coverage indicators. ICRA notes that this is in spite of the fact that GoR had taken over 75% of the debt of the distribution company (discom) over FY2016 and FY2017 under UDAY which has been gradually converted into a combination of grant and equity. ICRA also notes the qualified opinion in the audit report of AVVNL for FY2020.

The Stable outlook on this rating reflects ICRA's outlook on the rating of the guarantor, GoR.

### Adequacy of credit enhancement

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The rating of the instrument is based on the credit substitution approach whereby the rating of the guarantor has been translated to the rating of the said instrument. ICRA has reviewed the GoR Order and the term sheet for the proposed bonds. As per the said documents, the guarantee will be legally enforceable, irrevocable, unconditional, and will cover the entire amount and tenor of the rated instrument. Further, it will have a well-defined invocation and payment mechanism. Given these attributes, the guarantee to be provided by the GoR would be adequately strong to result in an enhancement in the rating of the said instrument to Provisional [ICRA]BBB(CE) against the Unsupported Rating of [ICRA]BB. However, ICRA has not been able to assess whether the guarantor would waiver off its rights under Sections 133, 134, 135, 139 and 141 of the Indian Contracts Act and the same would be a monitorable. In case the rating of the guarantor was to undergo a change in future, the same would reflect in the rating of the aforesaid instrument as well.

#### **Salient covenants of the proposed rated facility**

- » *DSRA to be maintained at all times and shall be equal to next debt servicing amount*
- » *In the event of default as defined in the draft transaction documents, the guarantor would cover the entire liabilities remaining outstanding on the rated bonds*

### **Key rating drivers and their description**

#### **Credit strengths**

**Corporate guarantee to be provided by GoR** - The rating for the proposed bond is based on the strength of the unconditional and irrevocable guarantee to be provided by GoR. It also draws comfort from a trustee-monitored payment mechanism which will ensure the timely payment of the interest and principal obligations on the bond programme.

**State ownership and support** - AVVNL came into existence post the unbundling of the erstwhile Rajasthan State Electricity Board (RSEB) in July 2000. It is responsible for distribution of power in Central Rajasthan and is strategically important to the state power sector. It is wholly owned by the GoR, which has supported the discom through regular infusion of funds in the form of equity, grants and guaranteed debt.

**Presence of fuel surcharge mechanism ensures pass through of cost variations; tariff hike should lower the revenue gap** - The fuel surcharge mechanism is operational for Rajasthan discoms, which allows them to recover in a timely manner such uncontrollable cost variation on quarterly basis with RERC's approval. Also, the RERC approved a tariff hike in the last tariff order dated February 2020 (last tariff hike implemented in September 2016). The increased tariff will lead to an improvement in the cash flows of the company and will also result in lower revenue gap for the discom going forward.

#### **Credit challenges**

**Moderately high loss levels; reduction seen post implementation of UDAY** - While AVVNL has achieved gradual improvement in the distribution loss levels over the past few years since the implementation of UDAY and has been able to meet the target of loss reduction set under UDAY and approved by RERC for FY2020, the loss levels still remain moderately high. The distribution loss stood at 14.48% in FY2020 and the AT&C loss also remained high at 21.99% (14.49% when adjusted for subsidy received) in FY2020.

**High levels of unpaid subsidy from GoR for previous years; subsidy dependence on the state remains high** - The absolute level of subsidy dependence on GoR for AVVNL remained high at ~Rs. 3,000 crore (21% of the revenue) in FY2020. While subsidy has been received on a monthly basis, the actual receipt from GoR has been much lower than that

claimed by AVVNL and as a result, outstanding subsidy from GoR built up to Rs. 2,738 crore over the years till March 31, 2020. The same is currently funded by debt and is a long-term concern.

**Weak financial profile** - The financial profile of AVVNL remains weak characterised by weak cost coverage ratio, high debt levels, negative networth and weak debt coverage indicators. The cost coverage ratio has remained in the range of 72-80% over FY2018-FY2020 which should improve with the implementation of the revised tariffs. Also, the overall debt levels remain high due to high unfunded revenue gap and the networth of the company remained negative as on March 31, 2020 due to large losses booked in the past. ICRA notes that this is despite the fact that GoR had taken over 75% of the debt of the discom over FY2016 and FY2017 under UDAY which has been gradually converted into a combination of grant and equity till FY2020. The debt service coverage indicator continues to remain below 1.0 time indicating refinancing requirement.

## Key rating drivers and their description for the guarantor (GoR)

### Credit strengths

**Revenue receipts dominated by Central transfers** - The GoR receives substantial Central transfers, which augment its revenue receipts. Central transfers comprised ~48% of the revenue receipts of the state government during FY2016–FY2019.

### Credit challenges

**Modest own tax effort** - The GoR's own tax revenues have declined from 6.3% of gross state domestic product (GSDP) in FY2016 to 6.1% in FY2019 and remain lower than several other states.

**High spending on power subsidy** - The GoR's power subsidy stood at 1-1.4% of GSDP during FY2016-FY2018, higher than most other states. Subsequently, the GoR's power subsidy allocation declined to Rs. 7,959 crore or 0.8% of GSDP in FY2019 from Rs. 11,391 crore or 1.4% of GSDP in FY2018.

**Unfavourable fiscal balances** - The GoR recorded a nearly five-fold increase in its revenue deficit to Rs. 28,900 crore or 3.1% of GSDP in FY2019 from Rs. 5,954 crore or 0.9% of GSDP in FY2016 led by support extended to the power sector, crop loan waiver in FY2019 and revision of salaries over the course of FY2018 and FY2019. A high revenue deficit resulted in the GoR's fiscal deficit exceeding the norms set by the Finance Commission (FC) in FY2016, FY2017 and FY2019.

**High leverage levels (debt + guarantees)** - Reflecting the sustained fiscal deficits and support extended to the power sector, the GoR's leverage levels stood at an unhealthy 37.2% of GSDP and at 6.1x of the state's own tax revenue (SOTR) in FY2019, higher than 36.0% of GSDP and 5.7x SOTR in FY2016.

### Liquidity position of GoR: Adequate

The GoR has availed the Ways and Means Advances and/or the Overdraft facilities from the Reserve Bank of India (RBI) on only a few occasions during FY2020 and FY2021 (till September 2020). Additionally, the GoR had an investment of Rs. 2,000 crore in auction Treasury-bills and Rs. 129 crore in Government securities at the end of September 2020. Based on the aforementioned indicators, the liquidity position of the state government can be inferred to be adequate in recent times.

## Rating sensitivities for AVVNL

The rating assigned to the proposed bonds would remain sensitive to any movement in the rating or outlook of the guarantor, GoR. Also, non-adherence to the guarantee structure could lead to a downward rating revision.

## Rating sensitivities for GoR

**Positive triggers** – Sustained improvement in the fiscal and leverage levels of the GoR could lead to an upward rating movement.

**Negative triggers** – Negative pressure on the rating could arise if there is relatively delayed recovery in the GoR's revenues, leading to prolonged adverse impact on its fiscal balance and leverage levels. Increase in the debt outstanding of the state power sector entities (either supported or unsupported by the GoR), leading to a significant worsening of the consolidated leverage levels of the state government and its power entities could also exert negative pressure on the rating.

## Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Rating Methodology for Power Distribution Utilities</a> <a href="#">Corporate Credit Rating Methodology</a> <a href="#">Approach for rating debt instruments backed by third-party explicit support</a>
Parent/Group Support	The rating is based on the unconditional and irrevocable corporate guarantee to be extended by GoR
Consolidation/Standalone	Not applicable, since the rating is based on the unconditional and irrevocable corporate guarantee to be extended by the GoR

## About the company

Government of Rajasthan unbundled the RSEB with effect from July 19, 2000. The Generation, Transmission and Distribution businesses of the erstwhile RSEB were transferred to five companies. The five successor companies were formed on functional lines into three discoms, one generation entity and one transmission entity as listed below:

<b>Generation company</b>	Rajasthan Rajya Vidyut Utpadan Nigam Limited (RRVUNL)
<b>Transmission company</b>	Rajasthan Rajya Vidyut Prasaran Nigam Limited (RRVPNL)
<b>Distribution companies</b>	Jaipur Vidyut Vitran Nigam Limited (JVVNL) Ajmer Vidyut Vitran Nigam Limited (AVVNL) Jodhpur Vidyut Vitran Nigam Limited JdVVNL)
<b>Power procurement intermediary</b>	Rajasthan Urja Vikas Nigam Limited (RUVNL)

AVVNL is an unbundled state power discom of RSEB. It is engaged in the distribution of electricity in 11 districts of Rajasthan namely Ajmer, Bhilwara, Nagaur, Sikar, Jhunjhunu, Udaipur, Banswara, Chittorgarh, Rajsamand, Doongarpur & Pratapgar.

In FY2020, the company reported a net profit of Rs. 754 crore on an operating income (OI) of Rs. 14,465 crore, compared to a net profit of Rs. 697 crore on an OI of Rs. 13,008 crore in the previous year.

## Key financial indicators of AVVNL (audited)

	FY2019	FY2020
Operating Income (Rs. crore)	13,008	14,465
PAT (Rs. crore)	697	754
OPBDIT/OI (%)	-2.2%	11.4%
RoCE (%)	-78.2%	-79.5%
Total Outside Liabilities/Tangible Net Worth (times)	-1.9	-2.6
Total Debt/OPBDIT (times)	-61.1	9.2
Interest Coverage (times)	-0.2	1.0
DSCR (times)	-0.1	0.8

## About the guarantor

Benefitting from large Central transfers (central tax devolution or CTD and grants from the Centre) as well as relatively higher state own non-tax revenues, the GoR's revenue receipts remained substantial at 14.2-15.1% of GSDP during FY2016-FY2019. Its revenue expenditure relative to GSDP rose from 15.4% each during FY2016-FY2017 to a high 17.3-17.6% during FY2018 to FY2019, led by the support extended to the power sector under the UDAY scheme, as well as social sector spending. This contributed to a considerable worsening of the GoR's revenue deficit from Rs. 5,954 crore or 0.9% of GSDP in FY2016, to Rs. 28,900 crore or 3.1% of GSDP in FY2019. Despite the decline in capital outlay and net lending from 2.5% of GSDP in FY2016 to 0.6% of GSDP in FY2019, the GoR's fiscal deficit exceeded the 14th FC's target of 3.0% of GSDP during all these years except in FY2018. Reflecting the sustained fiscal deficits as well as guarantees extended by the state government to the power sector, its leverage level remained adverse, rising to 37.2% of GSDP in FY2019 from 36.0% of GSDP in FY2016.

In its budget estimate (BE) for FY2021 (presented in February 2020), the GoR's revenue deficit was expected to narrow to Rs. 12,345 crore from Rs. 28,041 crore in FY2020 revised estimates (RE). This benefitted from the 10.6% expansion forecast in its revenue receipts in FY2021 BE relative to a low 0.5% in revenue expenditure. However, the consumption of several discretionary items, especially, tourism and hospitality sector, which is one of the key contributors to Rajasthan's economy, is expected to be adversely impacted in the ongoing fiscal by the Covid-19 pandemic. In ICRA's view, the consumption-based taxes of the state government would be sharply lower than budgeted in FY2021. Moreover, the demand shock related to the spread of Covid-19 would curtail the gross tax revenues of the Government of India (GoI) relative to the budgeted level, which would reduce the CTD to the states in FY2021.

To alleviate the fiscal and liquidity stress being experienced by the state governments due to the ongoing crisis, the GoI has permitted the states to borrow an additional 2% of GSDP in FY2021 (under option 1 of the two borrowing options proposed by the GoI, which has been chosen so far by a majority of the states), over and above the normal limit of 3% of GSDP. However, half of the additional borrowing that has been permitted (1% of GSDP), is conditional on the completion of the prescribed reforms by the state governments. Factoring in the additional unconditional borrowing that the GoR is allowed to undertake in FY2021 (1% of GSDP), we expect the indebtedness level of the state government to rise further in FY2021. With the rise in debt levels as well as the likely contraction in both the state own tax revenues or SOTR and in nominal GSDP in FY2021, the GoR's level of leverage relative to SOTR and GSDP is expected to deteriorate in the ongoing fiscal, which would worsen the fiscal profile of the GoR.

ICRA would continue to closely assess the impact of the Covid-19 pandemic on the GoR's revenues, both own and Central transfers, expenditures and its overall fiscal position. ICRA will monitor the timeliness and adequacy of the goods

and services tax (GST) compensation grants by the GoI to the states in FY2021, as well as the reform(s) that the state government is able to complete in the current fiscal, which would provide access to additional funds to bridge the anticipated gap between the expenditure and receipts. ICRA would also analyse the impact of the recommendations of the 15th FC for the award period FY2022-FY2026 on the GoR's finances.

### Key fiscal indicators of GoR (Amount in Rs. crore)

	FY2019	FY2020 RE	FY2021 BE
<b>Revenue</b>			
Revenue Receipts*	1,36,726	1,55,441	1,71,965
State's Own Tax Revenue	57,380	70,351	77,030
State's Own Non-Tax Revenue*	17,456	18,323	18,156
Share in Central Taxes	41,852	36,049	46,886
Grants from Centre	20,037	30,718	29,893
Capital Receipts <sup>&amp;</sup>	20	25	30
<b>Expenditure</b>			
Revenue Expenditure <sup>@</sup>	1,65,626	1,83,482	1,84,310
Capital Outlay	19,638	17,689	21,619
Net Lending	-14,045	-13,491	-12
<b>Revenue &amp; Fiscal Balance</b>			
Revenue Balance	-28,900	-28,041	-12,345
Fiscal Balance	-34,473	-32,214	-33,923
<b>Leverage</b>			
Debt	2,80,517	3,07,710	3,38,485
Guarantees	70,430		

Note: Contra entries related to UDAY loans include a provision of Rs. 12,000 crore and Rs. 13,816 crore, respectively, in FY2019 and FY2020 RE as grants (included under revenue expenditure) and Rs. 3,000 crore and Rs. 905 crore, respectively, in FY2019 and FY2020 RE as equity (included under capital outlay) to the Discoms offset by recovery of equivalent amount of loans from the Discoms.

\* Adjusted for double entries of interest from Departmental Commercial Undertakings

Source: State Budget, Finance Accounts and ICRA research

### Status of non-cooperation with previous CRA: Not applicable

### Any other information: None

### Rating history for past three years

S. No.	Instrument	Type	Current Rating (FY2021)		Date & Rating	Chronology of Rating History for the past 3 years		
			Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)		Date & Rating in FY2020	Date & Rating in FY2019	Date & Rating in FY2018
					14-Jan-2021	-	-	-
1	Proposed Bonds	Long term	500.00	-	Provisional [ICRA]BBB(CE) (Stable)	-	-	-

### Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website [www.icra.in](http://www.icra.in)

### Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Proposed Bonds	NA	NA	NA	500.00	Provisional [ICRA]BBB(CE)(Stable)

Source: Ajmer Vidyut Vitran Nigam Limited

### Annexure-2: List of entities considered for consolidated analysis: Not applicable

## Analyst Contacts

**Sabyasachi Mazumdar**

+91 124 4545 304

[sabyasachi@icraindia.com](mailto:sabyasachi@icraindia.com)

**Girishkumar Kadam**

+91 22 6114 3441

[girishkumar@icraindia.com](mailto:girishkumar@icraindia.com)

**Ankit Patel**

+91 79 4027 1509

[ankit.patel@icraindia.com](mailto:ankit.patel@icraindia.com)

**Parth Shah**

+91 79 4027 1527

[parth.shah@icraindia.com](mailto:parth.shah@icraindia.com)

## Relationship Contact

**L Shivakumar**

+91 22 6114 3406

[shivakumar@icraindia.com](mailto:shivakumar@icraindia.com)

## MEDIA AND PUBLIC RELATIONS CONTACT

**Ms. Naznin Prodhani**

Tel: +91 124 4545 860

[communications@icraindia.com](mailto:communications@icraindia.com)

## Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

[info@icraindia.com](mailto:info@icraindia.com)

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## ICRA Limited

### Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: [info@icraindia.com](mailto:info@icraindia.com)

Website: [www.icra.in](http://www.icra.in)

### Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

### Branches

Mumbai + (91 22) 24331046/53/62/74/86/87

Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,

Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,

Bangalore + (91 80) 2559 7401/4049

Ahmedabad+ (91 79) 2658 4924/5049/2008

Hyderabad + (91 40) 2373 5061/7251

Pune + (91 20) 2556 0194/ 6606 9999

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